

IN THE UNITED STATES DISTRICT COURT FOR THE  
SOUTHERN DISTRICT OF IOWA  
CENTRAL DIVISION

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DAVID E. WATSON, P.C.,

Plaintiff,

v.

CASE NO. \_\_\_\_\_

UNITED STATES OF AMERICA,

Defendant.

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**COMPLAINT**

COMES NOW, the Plaintiff, David E. Watson, P.C. (hereinafter "Watson PC"), and in support of its Complaint, states:

1. Watson PC is an Iowa professional corporation with its principal place of business at 801 57<sup>th</sup> Place, West Des Moines, Iowa 50266.
2. Defendant is the United States of America.
3. This is an action for the recovery of FICA tax, interest and penalty erroneously or illegally assessed and collected, and this Court has jurisdiction by reason of 28 U.S.C. §1346(a)(1).
4. Recovery is sought of FICA taxes for the calendar quarter ended December 31, 2002.
5. Watson PC was incorporated on October 11, 1996, by the filing of its Articles of Incorporation with the Secretary of the State of Iowa.

5. David E. Watson ("Watson") is employed by Watson PC pursuant to the terms of an Employment Agreement among Watson, Watson PC and Larson, Watson, Bartling and Juffer, L.L.P. ("Partnership") dated October 11, 1996.

7. Watson PC is a partner in the Partnership as set forth in the Registered Limited Liability Partnership Agreement dated October 11, 1996.

8. Watson is not, individually, a partner of the Partnership.

9. Watson is not employed by the Partnership.

10. On or about February 5, 2007, Defendant assessed additional employment taxes against Watson PC for the calendar quarters ended March 31, 2002; June 30, 2002; September 30, 2002; December 31, 2002; March 31, 2003; June 30, 2003; September 30, 2003; and December 31, 2003; representing FICA taxes allegedly due from Watson PC after Defendant determined that it would reclassify dividends paid to Watson and loans made to Watson as wages to Watson.

11. On or about April 11, 2007, Watson PC paid to the Defendant the sum of \$4,063.93, representing the additional tax and related penalty and interest assessed by Defendant against Watson PC with respect to the calendar quarter ended December 31, 2002.

12. The payment of \$4,063.93 was received by the IRS on or about April 14, 2007, and despite the fact that the payment was clearly designated for the fourth quarter of 2002, the payment was erroneously applied to the tax liability assessed with respect to the first quarter of 2002.

13. On or about June 27, 2007, Watson PC filed its claim for refund with respect to the tax, penalty and interest paid for the calendar quarter ended December 31, 2002. A copy of that claim is attached hereto as Exhibit "A", and made a part hereof.

14. On or about November 16, 2007, the Defendant, through its agency the Internal Revenue Service, denied Watson PC's claim for refund. A copy of the denial of claim is attached hereto as Exhibit "B".

15. During the calendar year 2002, Watson PC paid compensation in the amount of \$17,328 to Watson.

16. Wage payments of \$17,328 in 2002 were made through Merit Resources, Inc. who served as a "Principal Employer Organization" with respect to Watson PC.

17. Because Watson PC had elected "S Corporation" status, earnings of Watson PC in the amount of \$75,672 were taxed to its sole shareholder, Watson, in 2002.

18. Defendant erroneously determined that the dividend distributions of \$118,159 and a loan of \$81,743 made to Watson from Watson PC should, after deducting a "return on investment" of \$7,913, be treated as additional wages, resulting in the erroneous assessment and collection of additional Social Security and Medicare taxes in the amount of \$2,474.02 and related penalty and interest with respect to the calendar quarter ended December 31, 2002.

19. The Defendant based its reclassification of dividends and loans as wages upon its determination that the wages paid by Watson PC to Watson in 2002 did not constitute "reasonable compensation" as that term is utilized in Treas. Reg. §1.162-7.

20. Watson PC properly and legally declared dividends to be paid during the calendar year 2002 to its shareholder, Watson.

21. Watson PC properly and legally loaned funds in 2002 to its shareholder, Watson.

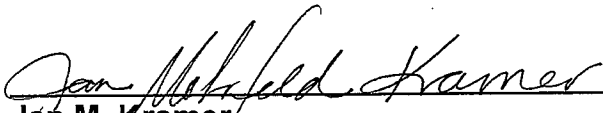
22. Watson PC has overpaid Social Security and Medicare taxes for the calendar quarter ended December 31, 2002, in the amount of \$2,474.02, plus related penalty and interest.

**WHEREFORE**, Watson PC requests judgment in the amount of \$4,063.93, plus interest and costs allowed by law, and such other relief as the Court may deem just, including the award of reasonable litigation costs incurred in this proceeding pursuant to 26 U.S.C. §7430.

Respectfully submitted,



**Ronald L. Mountsier**  
**PK0007647**



**Jan M. Kramer**  
**PK0013030**

SMITH, SCHNEIDER, STILES & SERANGELI, P.C.  
604 Locust, Suite 1000  
Des Moines, IA 50309  
Phone: 515-245-6789  
Fax: 515-244-1328  
Email: [rmountsier@smithlawiowa.com](mailto:rmountsier@smithlawiowa.com)  
[jmk@smithlawiowa.com](mailto:jmk@smithlawiowa.com)

ATTORNEYS FOR WATSON PC

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